Agenda Date: 01/31/02
Agenda Item: 2A

STATE OF NEW JERSEY

Board of Public Utilities

Two Gateway Center
Newark, NJ 07102

ENERGY

IN THE MATTER OF THE PETITION OF	)	
ATLANTIC CITY ELECTRIC COMPANY	)	DECISION AND ORDER
REGARDING THE SALE OF CERTAIN	)	
FOSSIL GENERATION ASSETS	)	DOCKET NO. EM00020106

(SERVICE LIST ATTACHED)

BY THE BOARD:

This matter concerns a petition dated February 9, 2000, filed by Atlantic City Electric Company ("ACE" or "Company"), requesting that the Board of Public Utilities ("Board") approve the sale of the Company's 100% interest in the B.L. England Generating Station ("B.L. England"), its 3.83% interest in the Conemaugh Generating Station ("Conemaugh")[1] its 2.47% interest in the Keystone Generating Station ("Keystone")[2] and related assets to NRG Energy, Inc. ("NRG"), as well as the recovery of resultant stranded costs and other related findings. ACE is also requesting a limited finding by the Board relating to the sale of the Company's 100% interest in the Deepwater Station ("Deepwater") to NRG. The Board had previously authorized ACE to transfer Deepwater to an affiliate of the Company, subject to certain conditions, in its Final Decision and Order ("Final Order"), dated March 30, 2001, In the Matter of Atlantic City Electric Company - Rate Unbundling, Stranded Cost and Restructuring Filings, Docket Nos. EO97070455, EO97070456 and EO97070457. The Company never transferred Deepwater to an affiliate, as authorized by the Board in its Final Order. The Company did not request Board approval of the sale of Deepwater to NRG in its instant petition. Hereafter, unless otherwise specified, the aforementioned generation assets, consisting of B.L. England, Conemaugh, Keystone and Deepwater and related assets, shall be referred to collectively as the "Fossil Assets".

Procedural History

In May 1999, Conectiv[3] announced that it intended to sell certain nuclear and fossil generation assets owned by its wholly owned utility subsidiaries, ACE and Delmarva Power & Light Company ("Delmarva").[4] Conectiv indicated that its decision to divest ACE's and Delmarva's

[1] Conemaugh is jointly owned by ACE, Baltimore Gas & Electric Company, Delmarva, Pennsylvania Power & Light Company, PECO Energy, Potomac Electric Power Company, Sithe Energies, Inc., and UGI Utilities, Inc.

[2] Keystone is jointly owned by ACE, Baltimore Gas & Electric Company, Delmarva, Pennsylvania Power & Light Company, PECO Energy, Public Service Electric and Gas Company, and Sithe Energies, Inc.

[3] Conectiv is a registered holding company under the Public Utility Holding Company Act ("PUHCA").

[4] Delmarva is an electric utility serving parts of Delaware, Maryland and Virginia.

generation assets was motivated by, among other things, the development of an active market for the sale of electric generation units, its strategic business plans, and the passage of the Electric Discount and Energy Competition Act ("EDECA" or "Act"), N.J.S.A. 48:3-49 et seq.

On August 11, 1999, the Company filed a petition with the Board, pursuant to N.J.S.A. 48:3-59(b), seeking approval of auction standards for the sale of certain of its fossil and nuclear generation assets, In the Matter of the Request of Atlantic City Electric Company for the Establishment of Auction Standards for the Sale of Certain Generating Units, Docket Nos. EM99080605 and EM99080606. At its September 19, 1999 public agenda meeting, the Board approved auction standards to be applicable when the Company sought Board approval of the sale of its fossil and nuclear generation assets. On January 4, 2000, the Board issued its Order Adopting Auction Standards ("Auction Standards Order"). Among other things, the Auction Standards Order established principles for maximizing the sales price, continuing environmental stewardship, mitigating the impact on the incumbent workforce, and maintaining the reliability of the electric system. The Auction Standards Order required ACE to submit a petition for approval of any proposed sale of its generation assets at the conclusion of the auction, at which time the Company must demonstrate compliance with the Auction Standards Order, as well as other applicable laws, regulations and policies.

On May 13, 1999, Conectiv initiated its auction process for the sale of its minority interest in the Fossil Assets with the mailing of approximately 1200 early interest letters to industry contacts around the world. The next step in the auction process, based on a response of 76 entities to the early interest letters, was the execution of confidentiality agreements, as well as a request for qualifications from those parties who expressed an interest in the purchase of the Company's interest in the Fossil Assets. Forty-one parties were willing to do so and were determined to be qualified bidders by the Company. In the next phase of the auction process, from about July 1999 to August 1999, the Company issued detailed offering memoranda and a CD-ROM[5] to the 41 entities that executed confidentiality agreements. On August 16, 1999, 14 parties submitted indicative bids which the Company, upon evaluation of the parties' price, financial strength, experience, exceptions to the terms of the sale and their coverage for each asset offered, reduced to ten bidders. On December 8, 1999, five final bids were received.

By petition dated November 23, 1999, in Docket No. EM99100870, ACE requested that the Board approve the sale of the Company's minority interest in the Salem Nuclear Generating Station, Units I and 2, the Peach Bottom Atomic Power Station, Units 2 and 3, and the Hope Creek Nuclear Generating Station (collectively, "Nuclear Assets"), to PSEG Power LLC and PECO Energy Company, as well as the recovery of resultant stranded costs and other related findings. By Decision and Order dated July 21, 2000, the Board approved the sale of the Nuclear Assets, In the Matter of the Petition of Atlantic City Electric Company for Approval of the Sale of its Nuclear Generating Assets. By Decision and Order dated September 17, 2001 in the same docket, the Board determined the recovery-eligible amount of stranded costs associated with the sale of the Nuclear Assets.

On January 18, 2000, ACE entered into two separate Purchase and Sale Agreements ("PSAs") with NRG for the sale of the Company's interest in the Fossil Assets to NRG for approximately $178.4 million, subject to certain adjustments. NRG is a subsidiary of Northern States Power Company, headquartered in Minneapolis, Minnesota. NRG is an independent power producer

[5] The CD-ROM included data relating to the Fossil Assets as part of this sale.

having interests in generation facilities in the United States and other countries. NRG owns generation capacity in the New York Power Pool, the New England Power Pool and the PJM Interconnection LLC ("PJM").

One PSA concerns the sale of B.L. England and Deepwater ("PSA1"), while the other PSA concerns the sale of ACE's minority interest in Conemaugh and Keystone ("PSA2"). The PSAs anticipated a closing on or about September 1, 2000. In the event that all conditions to the closing were met but the required regulatory approvals were not obtained by January 18, 2001, the PSAs provided that either ACE or NRG could terminate the agreements on or after June 17, 2000. As described below, these dates were later extended by mutual agreement of ACE and NRG.

On February 9, 2000, the Company filed a petition with the Board requesting approval of the sale of its Fossil Assets to NRG, pursuant to N.J.S.A. 48:3-7 and N.J.S.A. 48:3-49 et seq. The Company requested a finding by the Board that it may recover the eligible stranded costs associated with the sale of the Fossil Assets, pursuant to N.J.S.A. 48:3-61(a)(1), as well as a finding by the Board that it may issue transition bonds to recover the total amount of the eligible stranded costs associated with the sale of the Fossil Assets, pursuant to N.J.S.A. 48:3-62(c)(1). The Company further requested certain findings to enable both ACE's Fossil Assets as well as certain of Delmarva's generation assets that were to be sold to NRG, to be considered "eligible facilities" pursuant to Section 32 of the Public Utility Holding Company Act ("PUHCA"). PSA1 and PSA2 were attached to the petition as Exhibit A and Exhibit B, respectively. A summary of ACE's proposed stranded costs relating to the Fossil Assets was attached to the petition as Exhibit C.

On March 29, 2000, the Board adopted a procedural schedule to allow interested parties the opportunity to review and provide input to the Board regarding the proposed sale of the Company's Fossil Assets to NRG. The parties to the proceeding included Conectiv, ACE, Board Staff, and the Division of the Ratepayer Advocate ("Advocate").[6] The procedural schedule included an opportunity for the parties to propound discovery, participate in a public/legislative-type hearing, and submit post-hearing comments and reply comments to the Board. On June 7, 2000, the Board revised the procedural schedule to allow additional time for the parties to provide additional discovery and extended the remaining procedural schedule accordingly. Both Board Staff and the Advocate propounded discovery on the Company.

On June 22, 2000, a public/legislative-type hearing was held at the Board, before Commissioner Frederick F. Butler, regarding the pending sale of the Company's Fossil Assets to NRG. At the hearing, the Company presented testimony by Thomas S. Shaw, Executive Vice President of the Company and its parent company, Conectiv; Donna Powell, Financial Services Coordinator for Conectiv; Charles Mannix, Manager of Taxes for Conectiv; and James M. Coyne, Managing Director, Navigant Consulting. Board Staff and the Advocate questioned the Company's witnesses on a number of issues regarding the proposed sale to NRG, including the sale process, the sale price and reliability issues. At the hearing, the Advocate opposed the Company's petition and expressed its concerns with respect thereto to the Board. The Advocate argued that full evidentiary hearings were needed in this matter. The Advocate also expressed a concern over the absence of a parting contract between ACE and NRG for the sale of power to ACE, similar to an agreement that had been negotiated between NRG and Delmarva. The Advocate asserted that the absence of such an agreement exposed ACE's

[6] As discussed later, NRG also became a party when the Board reopened the record in this matter for additional proceedings.

customers to undue supply and price risks during the transition to a fully competitive supply market.

On July 7, 2000, the Board received written comments from the Company and the Advocate, Both parties filing reply comments with the Board on July 14, 2000. The comments and reply comments are summarized later in this Order.

On April 12, 2001, the Company amended its filing in this matter to include a proposed Master Power Purchase and Sale Agreement ("PPA") between itself and NRG Power Marketing Inc., an affiliate of NRG, for the purchase by ACE of 400 megawatts ("mW") of unforced capacity and 400 megawatt-hours ("mWh") of continuous firm energy from NRG Power Marketing Inc. for the period commencing on the closing on the sale through August 31, 2002. By letter dated April 16, 2001, the Company supplemented its amended filing with additional documentation relating to the PPA.

By letter dated May 25, 2001, the Advocate provided its comments regarding the PPA. The Advocate asserted that the terms of the PPA compared poorly to those of the parting contract that NRG had negotiated with Delmarva at the time of the sale of Delmarva's fossil assets. The Advocate asserted that New Jersey customers would receive even less value from the sale as the result of the costs associated with the PPA, and that the terms of the PPA were not prudent or reasonable. The Advocate also asserted that the amount of contracted energy and capacity, and the duration of the PPA through August 31, 2002, would not adequately protect customers.

By letter dated June 12, 2001, ACE responded to the Advocate's comments. ACE asserted that obtaining full market value for Fossil Assets necessarily precluded an opportunity to obtain a below-market parting contract from NRG Power Marketing Inc. at the time of the sale of the Fossil Assets. The Company asserted that it initially intended to rely upon its basic generation supply ("BGS") procurement process, conducted under the oversight of the Board, to meet its ongoing BGS requirements. ACE further asserted that, in recognition of the Advocate's concerns regarding the absence of a parting contract, the approach of the summer season and the possibility of Board consideration of the instant petition prior thereto, the Company had negotiated the PPA with NRG.

At its public agenda meeting on June 20, 2001, on its own motion, the Board determined to bifurcate the Company's petition and rule upon the Company's request that the Board make certain findings to enable Delmarva's ownership interest in certain fossil generation assets being sold to NRG to qualify for eligible facilities status under Section 32 of PUHCA. Delmarva's fossil generation assets that were being sold to NRG consisted of Delmarva's interest in Conemaugh, Keystone, the Indian River Station ("Indian River") and the Vienna Station ("Vienna") (collectively, "Delmarva Fossil Assets"). The sale of the Delmarva Fossil Assets did not require Board approval since Delmarva is not a New Jersey public utility. By order dated June 21, 2001, the Board determined that allowing the Delmarva Fossil Assets to be eligible facilities, pursuant to Section 32 of PUHCA, will benefit New Jersey consumers, is in the public interest and does not violate State law.

By letter dated June 29, 2001, ACE advised the Board that, effective June 22, 2001, the Company had agreed to alter its agreements with NRG and NRG Power Marketing Inc. ACE and NRG amended the PSAs to provide for the separate sale by ACE of its interests in each of the Fossil Assets. ACE and NRG also amended their PSAs to provide for the extension of the termination dates of PSA1 to October 31, 2001 and PSA2 to December 31, 2001. Lastly, ACE

and NRG Power Marketing Inc. terminated their PPA because, according to ACE, the PPA was no longer appropriate due to the passage of time.

By letter dated July 27, 2001, ACE advised Board Staff that the Company had received a letter dated July 11, 2001 from the New Jersey Department of Environmental Protection ("DEP") advising ACE that the DEP had denied the Company's request to continue to burn up to 2.6 percent sulfur coal at Unit 1 of B.L. England after July 31, 2001. While ACE indicated that it was trying to resolve this matter with the DEP, the Company expressed concern that any continued operation of Unit 1 beyond that date would violate DEP permit requirements.

By letter dated July 30, 2001, ACE advised the Board that, on July 27, 2001, the DEP issued a 60-day stay of its fuel permit denial. By further letter dated August 2, 2001, ACE updated Board Staff on the operational status of Unit 1.[7]

At its public agenda meeting on October 25, 2001, on its own motion, the Board determined to reopen the record in this matter for additional proceedings before ruling on the Company's outstanding requests with respect to its petition. Specifically, the Board determined that additional proceedings, including an evidentiary hearing, would be necessary to: (1) supplement and update the record as to whether the proposed sale price of the Fossil Assets reflects the current market price; (2) review the fuel permit situation at B.L. England; and (3) provide the Company an opportunity to explain why it was proposing to sell its interest in Deepwater to NRG rather than transferring the facility to an affiliate, as the Company had previously requested Board approval to do and which proposed transfer was approved by the Board with modifications and subject to certain conditions in the Final Order. The Board established a supplemental procedural schedule for the filing of additional testimony by the parties, including the opportunity to propound discovery, submit testimony cross-examine witnesses in an evidentiary hearing, and submit post-hearing comments and reply comments to the Board. The Board's actions were memorialized in a letter by the Board Secretary dated October 25, 2001.

On November 7, 2001, ACE filed supplemental testimony and exhibits. Among other things, the supplemental testimony included additional amendments to the PSAs between ACE and NRG, extending the agreements through February 28, 2002. The testimony also provided information relating to the permit status of B.L. England and the proposed transfer of Deepwater to NRG.

The Advocate propounded discovery with respect to the Company's supplemental filing. On December 3, 2001 and December 4, 2001, the Advocate filed confidential and redacted versions of its supplemental testimony, respectively. On December 11, 2001, an evidentiary hearing was held at the Board, presided over by Commissioner Frederick F. Butler,[8] regarding the pending sale of the Company's Fossil Assets to NRG. At the hearing, the Company presented supplemental testimony by Thomas S. Shaw and James M. Coyne, as well as testimony by D. Bruce McClenathan, Director of Generation for Conectiv, Mark W. Finfrock, Director of Risk Management for Conectiv, Craig A. Mataczynski, President and Chief Executive Officer of NRG North America, and F. Reed Wills, Vice President, Mid-Atlantic Region of NRG North America. The Advocate presented testimony by Paul Chernick of Resource Insight, Inc. The Company, Board Staff and the Advocate cross-examined the witnesses. The Company and the Advocate filed initial supplemental comments on December 21, 2001 and reply

[7] As described in more detail later in this Order, subsequent 60-day stays have been issued by the DEP. The DEP has also issued a certificate to operate Unit 1 until June 2002, as well as a permit addendum to test burn lower sulfur coal.

[8] Then-President Connie O. Hughes also attended portions of the hearing.

comments on January 4, 2002. NRG also filed comments on January 4, 2002 in response to the Advocate's initial comments. The supplemental testimony, supplemental comments and supplemental reply comments are summarized later in this Order.

Summary of the Company's Petition

1) Terms of the Proposed Fossil Assets Sale

According to PSA1, NRG has agreed to pay approximately $82.3 million for ACE's wholly owned B L. England and Deepwater facilities, of which $68.5 million is attributable to the sale of B.L. England and $13.8 million to the sale of Deepwater. According to PSA2, NRG has agreed to pay approximately $96.1 million for ACE's interest in Conemaugh and Keystone.

The Company will convey to NRG, subject to certain exclusions set forth in the PSAs: (1) title and interest in, to and under all of the Fossil Assets, including, among other things, the real property upon which the Fossil Assets are sited, all inventories, machinery, equipment, contracts, vehicles, fixtures and furniture, transferable permits, all books, records and operating manuals, agreements relating to the ownership, operation or maintenance of such assets and transferable warranties and guarantees; (2) certain emission allowances; and (3) certain Merrill Creek Reservoir Project interests ("Merrill Creek").[9]

Pursuant to the PSAs and the Auction Standards Order, NRG will assume all pre-closing, onsite environmental liabilities associated with the Fossil Assets. NRG will also assume all post-closing, on-site and off-site environmental liabilities associated with the Fossil Assets. The Company asserts that the assumption of these liabilities by NRG will lower ACE's long-term exposure to the risk of potentially costly environmental clean-up liability.

The Company asserts that, as a result of the sale and in accordance with the Auction Standards Order, there will be minimal impact on the employees working at the Company's wholly owned generation facility. Pursuant to PSA1, NRG will offer employment to all union employees working at B.L. England, pursuant to the applicable employee bargaining agreements in effect at the time of closing of the sale. NRG shall hire its initial management personnel complement from among the non-union employees working at the generation facilities, but shall not be required to offer employment to all said non-union employees. Since the Company has no employees associated with Conemaugh and Keystone, PSA2 does not contain any provisions relating to employees.

2) Stranded Costs Estimate

ACE seeks a determination by the Board as to the quantification of the Company's eligible stranded costs associated with sale of the Fossil Assets, excluding Deepwater, defined by N.J.S.A. 48:3-51 as "the amount by which the net cost of an electric public utility's electric generating assets…, as determined by the [B]oard consistent with the provisions of this [A]ct, exceeds the market value of those assets…in a competitive supply marketplace…". Pursuant to

[9] Merrill Creek, located in Harmony Township, New Jersey, was developed by ACE and the other co-owners of Merrill Creek in the mid-1980s to provide compensation releases to the Delaware River, pursuant to the requirements of the Delaware River Basin Commission, to compensate for the Delaware River Basin water consumed during times of drought by the electric generation stations situated in the Delaware River Basin. Merrill Creek consists of a 650-acre reservoir with about 48,000 acre-feet of water storage capacity on approximately 2,000 acres of real estate, a dam, dikes, a pump house, pumps, pipeline and related works and appurtenant equipment and facilities.

N.J.S.A. 48:3-61(a)(1), ACE also seeks a finding by the Board that the Company may recover such eligible stranded costs. Lastly, ACE seeks a finding by the Board, pursuant to N.J.S.A. 48:3-62(c)(1), that the full amount of eligible stranded costs either may constitute, or be included as part of, the principal amount of transition bonds for which the Company may seek approval to issue under the Act.

As discussed above, ACE is not seeking any stranded cost recovery associated with Deepwater. In its Final Order, the Board adopted, with modifications, a stipulation of settlement between ACE and certain other parties to the Company's rate unbundling, stranded cost and restructuring proceedings. In the Final Order, the Board modified the stipulation of settlement to permit the transfer of Deepwater to an affiliate at the book value of the facility. Also pursuant to the terms of the Final Order, the Company will not be permitted to recover any net stranded costs associated with Deepwater.

In quantifying its estimated stranded costs, from the $178.4 million sale price received for the Fossil Assets less the $13.8 million sale price for Deepwater, netting $164.6 million, the Company deducted estimated transaction costs associated with the sale, the book value of the Fossil Assets, construction work in progress, fuel and other inventories, construction and other advances, and losses on reacquired debt. These deductions also exclude any adjustments associated with Deepwater. The Company's initial estimated quantification of stranded costs in the amount of $182.6 million was based on the book value of the Fossil Assets, less Deepwater, as of December 31, 1999. (Petition, Exhibit C). After updating to reflect the book value of the assets as of April 30, 2000, the estimate was reduced to $177.6 million (Exhibit C - Update No. 1, submitted in response to Board Staff discovery request BPU-13). In each case, the estimates do not reflect the tax reductions associated with the remaining tax basis of the units and other deductible costs. On a "net-of-tax" basis, the Company's updated stranded costs estimate based on the December 31, 1999 book value of the Fossil Assets, less Deepwater, is $105.0 million (Exhibit C – Update No. 1).[10]

Included among the items sought by the Company for recovery as stranded costs is a loss on reacquired debt. ACE is seeking recovery of a loss on reacquired debt associated with the Fossil Assets, less Deepwater, in an amount of approximately $4.1 million, net-of-tax, as of April 30, 2000. A loss on reacquired debt is incurred when higher cost debt is refunded with lower cost debt to take advantage of declining interest rates, which typically requires the upfront payment of a premium, or an amount above face value, on the redeemed bonds.

3) Eligible Facilities Determination

As part of its petition, the Company is requesting that the Board make certain findings pursuant to Section 32(c) of PUHCA, 15 U.S.C.A. §79z-5a(c), so that NRG can be considered for exempt wholesale generator ("EWG")[11] status under PUHCA. EWG status will exempt NRG from regulation under PUHCA.

[10] By letter dated July 5, 2001, ACE provided Board Staff with an informal update of Exhibit C, wherein the Company estimated the quantification of the stranded costs of the Fossil Assets, based on a book value as of March 31, 2001, to be approximately $161.7 million which, on a net-of-tax basis, is approximately $95.7 million.

[11] 15 U.S.C.A. §79z-5a defines an EWG as "any person determined by the [FERC] to be engaged directly, or indirectly through one or more affiliates …, and exclusively in the business of owning or operating, or both owning and operating, all or part of one or more eligible facilities and selling electric energy at wholesale…."

Since Conectiv is a registered holding company under PUHCA, in accordance with 15 U.S.C.A. §79z-5a(c), to qualify for EWG status, EWGs must be exclusively engaged in the business of owning or operating an eligible facility, as defined therein. ACE must obtain a specific determination from the Board that allowing the Fossil Assets to be eligible facilities will benefit New Jersey consumers, is in the public interest and does not violate New Jersey law. Specifically, in order for the Fossil Assets to be considered eligible facilities under 15 U.S.C.A. §79z-5a(c):

> [E]very State commission having jurisdiction over any such rate or charge must make a specific determination that allowing such facility to be an eligible facility (1) will benefit consumers, (2) is in the public interest, and (3) does not violate State law; [p]rovided, [t]hat in the case of such a rate or charge which is a rate or charge of an affiliate of a registered holding company:
>
> > (A) such determination with respect to the facility in question shall be required from every State commission having jurisdiction over the retail rates and charges of the affiliates of such registered holding company . . . .

On May 15, 2000, Conectiv and NRG filed a joint application ("Joint Application") with the Federal Energy Regulatory Commission ("FERC") seeking authorization for the sale of Conectiv's interest in the Fossil Assets to NRG. NRG asserts in the Joint Application that the sale of the Fossil Assets will promote competition by eliminating a vertically integrated utility from the PJM marketplace. NRG asserts that it will participate in the wholesale sales and generation business, but not the transmission and distribution business, thereby promoting retail choice in the ACE service territory. NRG further asserts that, since it is acquiring less than 100% of the total Conectiv generation assets, NRG will not be able to exercise market power in PJM. NRG also asserts that, prior to divestiture, Conectiv's capacity ownership represented 6.7% of total PJM capacity while, after divestiture, NRG will have a 3.5% ownership of total PJM capacity. NRG concludes that a market concentration analysis is not required, as the divestiture of Conectiv's generation assets is deconcentrating in character and that the wholesale generation market will become more competitive with NRG's participation in PJM.

Both the petition and the Joint Application state that NRG will file an application with FERC for a determination of the status of the Fossil Assets as "eligible facilities" in order to obtain EWG status. A condition precedent to such a finding by FERC is the receipt of specific eligible facility determinations by all affected state public utility regulatory commissions. According to ACE, similar requests have been made to the appropriate regulatory authorities in Delaware, Maryland, Pennsylvania and Virginia, and all necessary regulatory determinations with respect to the Fossil Assets have been received, with the exception of New Jersey.

ACE asserts that the sale of its Fossil Assets will not result in undue market control by NRG, arguing that the combined 686 mW capacity of B.L. England and Deepwater is comparatively small in today's market. The Company further argues that its minority interest in Conemaugh and Keystone, representing 106 mW of capacity, will not create a significant shift in the generation marketplace. ACE asserts that the Company does not have undue market control in PJM, and that NRG currently has a limited presence in the PJM market.

Positions of the Parties

Company Initial Comments

In its initial comments, the Company asserts that it conducted the sale of its Fossil Assets in accordance with N.J.S.A. 48:3-59(c). The Company asserts the following: (1) Conectiv has obtained the full market value of the Fossil Assets; (2) the sale is in the best interest of the Company's customers; (3) the sale will not jeopardize the reliability of the electric power system; (4) the sale will not result in undue market power by NRG; (5) the impacts of the sale on workers at the generation units have been almost entirely mitigated; (6) the sale will carry out the Board-supported plan of Conectiv for divesting certain generation assets and determining stranded costs through a market-priced sale, with the process used by ACE consistent with the requirements set out in the Auction Standards Order; (7) the sale is not anticipated to adversely affect the status of employees currently employed at the facilities, the terms and conditions of their employment, or existing collective bargaining agreements;[12] (8) the sale will not impact the employees, as the Company does not have any employees at Keystone or Conemaugh, and NRG has agreed to offer employment to all bargaining unit employees and to retain most management employees at B.L. England and Deepwater, with the remaining management employees to be offered severance packages; and (9) NRG has offered generous signing bonuses to all employees who decide to remain with the facilities as NRG employees, with the bonuses ranging from $4,500 for bargaining unit employees to ten percent of base annual compensation for management employees, which represents a significant benefit to employees.

ACE asserts that the sale of the Fossil Assets is also fully consistent with the Board's Auction Standards Order as set forth in the record of this proceeding. ACE asserts that it conducted its auction process in a manner which yielded the highest market value while also considering such vital issues as system reliability, on-going environmental liabilities, operation safety, market power and impact on the workforce. The Company also asserts that the record demonstrates how the sale to NRG compares favorably with those results, and that the Company's decision to sell the Fossil Assets to NRG results in a purchase price which is clearly representative of the current market price for such assets.

ACE asserts that it attempted to negotiate a successful bid with the nominally highest bidder, but that it was unable to successfully negotiate terms that were acceptable to the Company and consistent with the Auction Standards Order. The Company asserts that, during its negotiations with the highest bidder, the bidder also attempted to reduce the purchase price.

ACE asserts that, as a result of the impasse with the first bidder, the Company began negotiations with the second highest nominal bidder, NRG. The Company asserts that, during the negotiations, NRG submitted an improved final bid, narrowing the difference between NRG's bid and the highest bid. The Company further asserts that as a result of its analysis of the improved NRG bid, and an evaluation of the prices, terms and conditions of other recent fossil assets sales, the Company determined to accept NRG's offer.

ACE asserts that it has established the recoverable level of stranded costs as a result of the divestiture of the Fossil Assets, which stranded costs should be approved by the Board as an

[12] Article VI, Section 6.8 of PSA1 sets forth the conditions relating to employees at Deepwater and B.L. England, including the assumption on closing by NRG of the Local 210 of the International Brotherhood of Electrical Workers ("IBEW") collective bargaining agreements.

amount eligible for securitization. The Company points out that the net stranded costs will be updated as of the closing of the transaction. The Company further notes that it is not seeking final approval of transition bonds at this time but, rather, an acknowledgement of its entitlement to issue such bonds for recovery of the full amount of eligible net stranded costs.

ACE asserts that the requested Board determinations under 15 U.S.C.A. §79z-5a(c) are appropriate to allow NRG to seek to qualify the Fossil Assets as eligible facilities and obtain EWG status. The Company also asserts that the requested determinations are consistent with the Board's Order, In the Matter of Atlantic City Electric Company's Rate Unbundling, Stranded Costs and Restructuring Filing, Docket Nos. EO9707455, EO9707456, EO9707457, dated July 15, 1999 ("Summary Order") regarding the sale of the Company's generation assets.

Advocate Initial Comments

In its initial comments, the Advocate stresses the need for evidentiary hearings in order to establish a comprehensive record upon which the Board can base its ruling in this matter, since the result of the sale will ultimately impact the rates paid by the Company's customers. The Advocate asserts that this matter is a contested case, as rates will ultimately be affected if the sale is approved and, therefore, requires an evidentiary hearing in order to cross-examine witnesses. The Advocate also asserts that this proceeding is a continuation of ACE's stranded costs recovery and restructuring and requires an evidentiary hearing under EDECA.

The Advocate argues that the sale is not in the public interest, and that the Board should not approve the transaction. The Advocate asserts that the Company has not maximized the sale price of its Fossil Assets and that the proposed sale includes an unreasonably low allocation of the sales proceeds to the Company's New Jersey jurisdictional assets, particularly with regard to B.L. England. The Advocate asserts that, if the sale were approved, the allocation would result in the Company's customers paying higher stranded costs surcharges. The Advocate also argues that ACE failed to fully consider a competing bid for the New Jersey units, which was more beneficial to its customers, and that the Company failed to complete the auction process by accepting NRG's offer to purchase the Fossil Assets for a price below full market value. The Advocate therefore argues that the Company's sale is not consistent with the Auction Standards Order. The Advocate further argues that the Company has an obligation to maximize the market value of its generation assets, and its New Jersey customers should be no worse off as a result of the divestiture then they would have been if the assets were not sold. The Advocate also argues that the Company failed to secure a "parting contract" with NRG to benefit its BGS customers by locking in reasonable prices for electricity through a negotiated power purchase agreement during the transition to full competition. The Advocate notes that Delmarva successfully secured a favorable parting contract with NRG as a condition of the sale of its interest in its generation assets. The Advocate contends that, if the sale is approved, the Board should adjust the allocation of the sales proceeds for ratemaking purposes, and that the stranded cost recovery associated with the Fossil Assets should be limited to an amount that reflects a reasonable allocation of the sales proceeds to B.L. England.

The Advocate opposes the requested "eligible facilities" determination as it relates to the sale of the Company's ownership interests. The Advocate asserts that ACE has not demonstrated how qualifying the Fossil Assets as eligible facilities will benefit New Jersey consumers or is in the public interest. The Advocate also asserts that ACE has not demonstrated that NRG will not have undue market control as a result of the purchase of the Fossil Assets, and that the Company should submit a market power analysis pursuant to the Auction Standards Order.

Lastly, the Advocate asserts that the proposed sale transaction may result in a double-recovery of the Company's loss on reacquired debt, absent an adjustment of the Company's distribution rates, as the loss on reacquired debt might be collected in both distribution and transmission rates.

Company Reply Comments

In its reply comments, ACE responded to the arguments raised by the Advocate. ACE asserts that a more than adequate factual record exists in this proceeding. The Company asserts that the Board followed proper procedures that were straightforward and thorough, and consistent with procedures used in other divestiture proceedings. ACE also asserts that the hearings conducted in this proceeding provided the Advocate an opportunity to question the Company's witnesses. Lastly, the Company argues that the Advocate also had an opportunity to present a witness, but chose not to do so.

ACE asserts that its auction process was conducted in a responsible manner, and in accordance with the Auction Standards Order and Board policy. ACE asserts that the auction process resulted in the Company obtaining the best price, and fair market value, for the Fossil Assets. ACE asserts that, of the bids received, the Company determined that the three lower bids, or combinations of the three lower bids, did not reach the level of the bids of NRG or the nominally high bidder. The Company asserts that it became clear to the Company that negotiations with the high bidder were not progressing and that the final bid was reduced twice from the initial level.

ACE asserts that its decision to accept NRG's next highest offer was based on the comparative merits of NRG and the nominally highest bidder, the course of the negotiations with each party, and the concern that, if the NRG proposal was rejected, the other bidder would further reduce its price or even not reach a final agreement, leaving the Company with much lower proposals from the remaining bidders.

ACE asserts that, when it decided to focus its negotiations on NRG as the successful bidder, the Company was not aware of NRG's allocation of its purchase price to the individual facilities. The Company asserts that its acceptance of NRG's offer was based on the comparative merits of the bids of NRG and the highest bidder and that the Company's goal was to achieve the best overall possible price for the Fossil Assets. The Company further asserts that NRG allocated the purchase price to B.L. England based on NRG's analyses of the Fossil Assets.

The Company asserts that the Advocate's proposed adjustments to NRG's allocation of the sales proceeds for ratemaking purposes have no basis in fact and should be rejected. ACE asserts that, throughout the Company's stranded costs and restructuring proceedings, the Advocate supported divestiture as the best way of providing an accurate measure of stranded costs, while now appearing to want to rely upon administrative estimates which it had previously argued against. ACE asserts that the recoverable level of stranded costs has been determined as a result of the Fossil Asset divestiture, and that the full stranded costs amount should be deemed as eligible for securitization.

ACE also asserts that the sale of the Fossil Assets will not result in market control by NRG. The Company asserts that, while the Advocate claims that not enough information has been provided to conclude that undue market control will not exist, the Advocate has not disputed the

fact that NRG does not have assets in the PJM market. The Company asserts that, in response to the Joint Application by Conectiv and NRG seeking authorization for the sale, FERC stated in its July 13, 2001 written approval, in Docket No. EC00-91-000 stated that: "[W]e find that the proposed transaction will not adversely affect competition." The Company therefore asserts that there is no basis for the Advocate to argue that the Board should consider there to be any market power concerns with this transaction.

ACE lastly asserts that the Advocate's opposition to the Board making certain determinations allowing NRG to be eligible for EWG status is unreasonable, as denial of eligible facilities status of the Fossil Assets would adversely affect the operation and sale of the output of the facilities. The Company asserts that the Board should reject the Advocate's arguments and make the requisite findings necessary for EWG status as required by PUHCA. The Company asserts that the Summary Order provides the basis for the requested determinations.

Advocate Reply Comments

In its reply comments, the Advocate responded to the ACE's initial comments, asserting that the Company has presented nothing that substantially refutes the arguments set forth in the Advocate's initial comments.

The Advocate maintains that ACE has not demonstrated that the proposed sale of the Fossil Assets is in the public interest and that the sale should not be approved. The Advocate reiterates its assertion that the sale price of the Fossil Assets does not reflect the full market value of ACE's New Jersey jurisdictional assets, and that an unreasonably low portion of the sales proceeds is allocated to B.L. England, adding to the stranded cost burden of the Company's customers. The Advocate asserts that the proposed sale does not meet the full market value test required by EDECA and that the Board should not approve the transaction. Alternatively, the Advocate asserts that the Board should adjust the allocation of the sale proceeds to B.L. England, thereby reducing the requested level of stranded costs that ACE may recover from its customers.

The Advocate continues to assert that ACE has failed to comply with the Auction Standards Order. The Advocate asserts that statements made by the Company's witnesses indicate that the auction process was prematurely cut short, resulting in a sale price that is below all reasonable calculations of the value of the Fossil Assets. The Advocate asserts the Company was under no obligation to sell its Fossil Assets if the offer price was too low and that, by pursuing the sale to NRG, the Company set in motion a series of events that negatively impact the Company's customers. Therefore, the Advocate asserts, the Board cannot make the necessary finding that the sale complied with the Auction Standards Order.

The Advocate maintains that ACE failed to secure a parting contract to ensure capacity and energy at a reasonable price for the Company's customers. The Advocate asserts that the Company did not timely comply with a Board directive to acquire capacity and energy to fulfill its BGS requirements and that it relied upon spot market purchases to meet its BGS requirements through May 31, 2000. The Advocate asserts that, as a result, ACE failed to obtain capacity and energy at a reasonable price for its customers. The Advocate asserts that Conectiv could and should have negotiated a PPA with NRG for ACE's customers as it did for Delmarva's customers. Therefore, the Advocate asserts that ACE should be required to procure a PPA with NRG under the same terms and pricing of Delmarva's PPA. Alternatively, the Advocate asserts

that ACE's customers should be given a credit through an adjustment to the allocation of the sales proceeds.

The Advocate recommends that, if the Board approves the sale, it should defer any final decision regarding the recoverable level of stranded costs as well as the eligibility of any particular level of stranded costs for securitization. The Advocate notes that ACE acknowledges that many of the cost items relating to the sale will not be fully determinable until some time after the closing of the sale. The Advocate asserts that, absent a review of the final numbers, the Board cannot make the necessary findings. Therefore, the Advocate recommends that the Board reserve the right to review the Company's final stranded cost calculation prior to finalizing the Company's recoverable stranded cost level attributable to the Fossil Assets.

The Advocate further submits that ACE's request for a determination that would permit the Company to recover the full amount of its eligible stranded costs associated with the Fossil Assets through the issuance of transition bonds is premature. The Advocate lastly submits that, once the Board determines a total level of ACE's recoverable stranded costs associated with the Company's fossil and nuclear assets, the Company may then file a petition for a bondable stranded cost rate order pursuant to EDECA.

The Advocate continues to assert that ACE has not provided any convincing support or record evidence upon which the Board can make the necessary findings regarding eligibility for EWG status for NRG. The Advocate asserts that ACE has not demonstrated how the Fossil Assets operating as eligible facilities will benefit customers or be in the public interest. Absent the receipt of more specific supporting information, the Advocate recommends that the Board deny or defer consideration of this issue.

The Advocate lastly submits that the Board should ascertain that ACE's stranded cost calculation reflects only its actual loss on reacquired debt cost, and that a portion of these costs is not included in the Company's regulated distribution and transmission rates.

Company Supplemental Testimony

As discussed above, ACE submitted supplemental testimony by six witnesses, consisting of three employees of the Company, two employees of NRG and a consultant to ACE.

Mr. Shaw testified in support of the sale of the Fossil Assets, the recovery of stranded costs associated with the sale, and the "eligible facility" determination for Deepwater (Exhibit P-5). Mr. Shaw's testimony also included amendments to the PSAs between ACE and NRG (P-5, Schedules TSS-1 and TSS-2), extending the dates of the PSAs through February 28, 2002.

Mr. Finfrock testified with respect to the issues raised by the Board concerning Deepwater (Exhibit P-6). Mr. Finfrock asserted that, pursuant to the Final Order, effective August 1, 1999, Deepwater has been excluded from any and all regulated cost recovery mechanisms. Mr. Finfrock asserted that: (1) ACE's customers no longer have any cost responsibility for the operation and maintenance of Deepwater; (2) Deepwater is operated in the open market; and (3) the Company's shareholders pay all of the costs associated with Deepwater. Mr. Finfrock asserted that, also pursuant to the Final Order, the transfer value of Deepwater shall be its book value, thereby resulting in zero stranded costs associated with the facility and fully mitigating the need for the Company to forego any related stranded cost recovery. Mr. Finfrock asserted that, even though Deepwater is included in the books and records of the Company, Deepwater's

costs, since August 1, 1999, are recorded "below the line" and, for ratemaking purposes, are not eligible for stranded cost recovery. Mr. Finfrock asserted that the process for transferring Deepwater began after the issuance of the Summary Order but that, prior to completing the transfer, Deepwater was included in the auction process. Mr. Finfrock further asserted ACE did not complete the transfer of Deepwater because the Company entered into an agreement to sell the facility to NRG before the transfer could be completed, and that there was no economic benefit to be gained by the Company or its customers from transferring Deepwater to an affiliate prior to consummation of the sale.

Mr. McClenathan testified as to the fuel permit situation at B.L. England (Exhibit P-7). Mr. McClenathan's testimony also included documentation relating to the fuel permit situation (P-7, Exhibit DBM-1). Mr. McClenathan described B.L. England as consisting of three steam turbines and four diesel generators, with Unit 1 and Unit 2 being coal fired, wet bottom, cyclone boilers installed in 1962 and 1964, respectively, and Unit 3 being an oil-fired boiler installed in 1974. Mr. McClenathan asserted that cyclone boiler technology was developed over 50 years ago as a means for using relatively low quality, high ash, high sulfur Midwestern bituminous coal to generate electricity. Mr. McClenathan asserted that B.L. England currently burns up to 2.6% sulfur coal which enables the cyclone boilers to operate efficiently. Mr. McClenathan asserted that B.L. England operates under a variety of air emissions permits and authorizations, and that renewal of Unit 1's fuel use authorization has been a primary source of recent environmental concerns at the facility.

Mr. McClenathan asserted that, in New Jersey, coal-burning facilities are generally required to burn coal with sulfur content less than or equal to 1% but that, if a facility owner can demonstrate, among other things, that the sulfur content of the coal being burned represents the minimum sulfur content that can be used by the facility and is reasonably available in sufficient quantity, the facility owner may be authorized by the DEP to burn higher sulfur coal for a five-year period, as was the situation at B.L.. England. Mr. McClenathan asserted that ACE received a five-year authorization in 1996 but that, upon requesting an additional five-year authorization, was notified by the DEP on July 11, 2001 that the Company's request was denied. Mr. McClenathan asserted that ACE appealed the DEP's decision and the DEP stayed the denial for sixty days, allowing Unit 1 to continue operating. Mr. McClenathan asserted that the DEP has issued a permit addendum and several stays that allow ACE to conduct a trial burn of different type of coal in Unit 1 and, during this period, to continue to burn 2.6% sulfur coal in Unit 1. The permit addendum and the current stay both expire on February 28, 2002.

Mr. McClenathan asserted that the trial burn is to help determine whether a lower sulfur coal, including a test coal from Utah, can be burned in Unit 1 without interfering with the normal operation of the cyclone boiler. Mr. McClenathan asserted that the initial trial burn series will cost ACE approximately $1 million, and that long-term cost and operational impacts, if any, from this environmental compliance activity are not known at this time. Mr. McClenathan asserted that a successful trial burn could result in more stringent fuel use requirements by the DEP and changes in facility operations which typically result in increased long-term operating costs.

Mr. McClenathan asserted that there are other potential environmental issues at B.L. England that are being evaluated by the Environmental Protection Agency ("EPA") and the DEP, with the results of these evaluations not yet known. Mr. McClenathan lastly asserted that, under the terms and conditions of PSA1 for B.L. England and Deepwater, NRG agreed to pay to clean up potential areas of environmental concern at both facilities, with the cost currently estimated to be approximately $3.5 million for B.L. England and $3 million for Deepwater.

Mr. Coyne testified as to the fair market value of the Fossil Assets (Exhibit P-8). Mr. Coyne's testimony also included information to support his assertions (Exhibits JMC-1 through JMC-6), as discussed below. Mr. Coyne asserted that the value to be received by ACE still represents the fair market value of the Fossil Assets. Mr. Coyne asserted that he considers the most relevant factors in ascertaining the current value of the Fossil Assets to be: (1) generation asset value as reflected in public auctions; (2) operating characteristics; (3) PJM electricity and coal prices; and (4) macroeconomic, financial and power market fundamentals. Mr. Coyne asserted that valuation analysts will typically refer to recent acquisitions of comparable assets and will often look to prices relative to generation capacity to better understand the overall market for the assets. Mr. Coyne asserted that, while average sale prices for generation assets have covered a wide range over the past several years, as shown in Exhibit JMC-1 of his testimony, average sale prices have been trending higher, with the Fossil Assets falling generally within the broad band of sale prices. Mr. Coyne asserted that it is difficult to ascertain a specific trend in generation asset sales with any precision, as various companies have been either divesting or acquiring generation assets, with some companies bidding aggressively for existing assets to quickly gain market share. Mr. Coyne also asserted that companies value generation assets on both an individual and portfolio basis, and these sales represent a broad array of fuel types, size, location and operating characteristics.

Mr. Coyne asserted that the Fossil Assets represent a mix of assets with widely differing market value, with the primary reasons for differing individual valuations of the individual assets being plant characteristics, size, location and the potential site value inherent in an existing facility. Mr. Coyne asserted that Keystone and Conemaugh are large, low heat rate units with low operating costs, while B.L. England and Deepwater are smaller, with operating and capital costs 3.2 times higher, and 2.9 times higher, respectively, than the average operating costs for Keystone and Conemaugh.

Mr. Coyne asserted that B.L. England is discounted, from a value perspective, because it has a relatively high heat rate, higher operating costs, and a higher nitrogen oxides ("NOx") output due to the cyclone configuration of Units 1 and 2. Mr. Coyne asserted that the negative impact of the cyclone technology on valuation is evident in data on the sale of similar units as shown in Exhibit JMC-2 of his testimony. Mr. Coyne asserted that the lower prices, in part, reflect buyers' awareness that cyclone-type boilers produce significantly higher NOx than boilers of other types, and therefore require higher levels of both operating cost and capital expenditure to meet increasing regulation of NOx output. Mr. Coyne asserted that fuel use and sulfur dioxide ("SO2") emissions inherent in cyclone boiler operations adversely affect value, typically by raising a buyer's estimate of future operating and capital costs. Mr. Coyne asserted that, if the test burn involving Utah coal at B.L. England is successful, and that coal becomes the source of coal for Unit 1, fuel costs would be likely to increase. Mr. Coyne also asserted that the market value of B.L. England is decreased if the facility is unable to offset the higher operating cost disadvantage with the use of lower cost, higher sulfur coal.

Mr. Coyne asserted that the current gross profit margin potential for a coal facility in PJM with B.L. England's heat rate and location has significantly declined in contrast to January 18, 2000, when ACE and BRG entered into PSA1 for B.L. England and Deepwater. Mr. Coyne asserted that a key indicator of the gross profit potential is the difference between spot electricity prices and spot fuel prices, or the "spark spread". Mr. Coyne asserted that, as reflected in Exhibit JMC-4, as of October 29, 2001, the spark spread is 57% lower than it was on January 18, 2000. Mr. Coyne asserted that, on a going forward basis, based on PJM futures price contracts and

coal spot prices, the current and near-term outlook for coal-based spark spreads is substantially reduced from two years ago.

Mr. Coyne asserted that macroeconomic, financial and power market fundamental factors have significantly changed and will likely have a negative impact on generation asset values. Mr. Coyne asserted that there is more caution regarding future investments in generation assets, citing an overall slowdown in the economy, which Mr. Coyne asserted is closely correlated with power demand. Mr. Coyne asserted that, as shown in Exhibit JMC-5, the economy shrank at an annual rate of 0.4% in the third quarter of 2001, which represents a considerable slowdown from the economic peak coincident with the timing of the sale of the Fossil, Assets to NRG. Mr. Coyne also asserted that, as shown in Exhibit JMC-6, the average valuation for five representative generation companies, including NRG, has fallen by over 50% during the second half of 2001. Mr. Coyne further asserted that fallout from power sector problems in California continues to raise doubts among generation investors regarding the future of electric deregulation in the United States.

Mr. Coyne concluded his testimony by asserting that he does not believe that a re-auction of the Fossil Assets would bring a higher value and that there is some risk that the premium obtained for the Fossil Assets in the original auction would be lost. Mr. Coyne asserted that the sale price offered by NRG reasonably approximates the current market value of the Fossil Assets and that, short of re-bidding the facilities to test current market conditions, the market parameters outlined in his testimony must be relied upon to make a reasoned judgment as to whether the originals auction results reasonably approximate a current market price for the facilities.

Messrs. Mataczynski and Wills testified as to the basis for NRG's bid to purchase the Fossil Assets (Exhibit NRG-1). The testimony of Messrs. Mataczynski and Wills also includes supporting information as set forth in Schedules NRG-1 through NRG-4. Messrs. Mataczynski and Wills asserted that, as shown in Schedule NRG-1, NRG currently has approximately 1,200 mW of capacity in the Mid-Atlantic region, with another 1,000 mW of generation capacity, including the Fossil Assets, under contract for purchase. Messrs. Mataczynski and Wills asserted that NRG's goal is to achieve a total of at least 10,000 mW of generation capacity in the Mid-Atlantic region, including PJM, by 2005.

Messrs. Mataczynski and Wills asserted that NRG recognized that the purchase of the Fossil Assets provided an immediate, substantial presence in PJM and that the location of the facilites on the eastern side of PJM, near load centers, provide expansion opportunities in New Jersey, Delaware and Maryland. Messrs. Mataczynski and Wills asserted that NRG also considered the future dispatch potential, fuel costs and other expenses and liabilities, including environmental concerns, of the Fossil Assets. Messrs. Mataczynski and Wills asserted that, in developing its bid for the Fossil Assets, NRG: (1) developed an internal forecast based upon unit heat rates, forward fuel pricing, load forecasts and pricing for electricity and installed capacity in PJM; (2) reviewed the operating history, expenses and costs associated with each facility; (3) evaluated tax exposures, environmental risks and other liabilities associated with each facility; and (4) compared the Fossil Assets to other generation purchases by NRG, and to other market sales.

Messrs. Mataczynski and Wills asserted that each of the generation facilities acquired by NRG, as shown in Schedule NRG-2, have specific characteristics that drive their inherent value, based primarily on their geographic location and the market in which they are located, as well as the fuel used, the age and size of the units and the technology utilized. Messrs. Mataczynski

and Wills asserted that Schedule NRG-3 provides bid prices for each generation facility purchased by NRG and that the purchase price for each facility was prepared by NRG without consultation with the seller. Messrs. Mataczynski and Wills asserted that one of the primary value indicators of a generation facility is the production cost of the facility, which is typically the primary factor in determining how often a facility will be utilized. Messrs. Mataczynski and Wills asserted that Schedule NRG-4 provides NRG's estimates of the individual production costs and capacity factors of the Fossil Assets.

Messrs. Mataczynski and Wills asserted that Keystone and Conemaugh are very competitive from a production cost standpoint, resulting in high capacity factors and base load operation, and commanding a premium in PJM. Messrs. Mataczynski and Wills asserted that B.L. England and Deepwater run on an intermediate basis and have higher production costs than any of NRG's regional units due to their location, size of the individual units and the technology used, all of which negatively impacts the bid price.

Messrs. Mataczynski and Wills asserted that energy prices and fuel prices change continually and affects valuation and that, if NRG reran its valuation now, the results would be different. Messrs. Mataczynski and Wills asserted that, of particular importance are the current environmental issues that have arisen at B. L. England that may make the facility more costly to operate or, in the worst case, be shut down as uneconomic. Messrs. Mataczynski and Wills asserted that, despite these risks, NRG believes that it can add value to B.L. England and Deepwater and make the facilities environmentally acceptable and competitive in the PJM market.

Advocate Supplemental Testimony

The Advocate submitted supplemental testimony by its consultant, Mr. Chernick (Exhibit RA-6). Mr. Chernick's testimony also includes supporting information as set forth in Schedules PLC-1 through PLC-5.

Mr. Chernick's Schedule PLC-2, lists asserted similar coal facility sales, including ACE's and other utilities' interests in Keystone and/or Conemaugh. Mr. Chernick asserted that the other sales were equal to, or somewhat higher than, the price bid by NRG, but that all sale prices are close to one another. Mr. Chernick therefore concluded that the prices assigned to Keystone and Conemaugh are reasonable. Mr. Chernick also testified that the price of Deepwater does not affect stranded costs and also appears to be reasonable.

Schedule PLC-3 of Mr. Chernick's testimony lists 19 transactions that Mr. Chernick asserted contained coal facilities that have been sold at market prices. Schedule PLC-4 graphically reflects the sale price of B.L. England on a dollars-per-kilowatt ("$/kW") basis, which Mr. Chernick asserted reflects the fact that allocated price of B.L. England is lower than any previous coal-dominated sale. Mr. Chernick asserted that Schedule PLC-4 is similar to Exhibit JMC-1, but that many sales listed in Exhibit JMC-1 have been removed, as they either contain no coal capacity or were listed more than once.

Mr. Chernick asserted that, of five sales of generation facilities with cyclone boiler configurations provided in Exhibit JMC-2, three sales are irrelevant to the determination of the market value of cyclone coal units, as two units were sold for book value in return for a long-term purchased power agreement and one facility's fuel was not coal. Mr. Chernick asserted that two remaining relevant sales, because of the timing of the sales, the units' ages and fuel types are sufficient to

explain the differences in the average prices of these sales. Mr. Chernick asserted that there is no evidence in Exhibit JMC-2 to support the assertion that cyclone units are selling for lower prices than other coal units.

Mr. Chernick asserted that Mr. Coyne's analysis of electricity prices and coal prices, contained in Exhibit JMC-4, resulted in an erroneous assertion regarding the spark spread for B.L. England. Mr. Chernick asserted that purchasers do not value generation facilities based on the market price of electricity on the day a sale agreement is signed but, rather, on projected market prices over a facility's remaining life. Mr. Chernick asserted that Mr. Coyne's comparison of a high-priced winter day to a low-priced fall day was flawed and that Mr. Coyne's analysis contains no long-term forecast of PJM market prices. Mr. Chernick also asserted that forward peak prices assumed by Mr. Coyne were not accurate. Mr. Chernick asserted that Exhibit JMC-4 also shows PJM market prices that were higher in October 2000 as the result of higher natural gas prices and that any comparison to October 2001 prices is irrelevant. Mr. Chernick also asserted that Mr. Coyne did not use actual coal prices for B.L. England, and that it is not clear whether the asserted price trends relate to a particular type of coal burned at B.L. England or that assumed delivery costs are representative of B.L. England.

Mr. Chernick asserted that prices for coal facilities have been stable or rising, as shown in Exhibit PLC-4, and that the sale of the Delmarva's fossil assets, including Indian River and Vienna, to NRG in June 2001 with an overall price of $548 $/kW, while B.L. England is priced at $153/kW. Mr. Chernick asserted that, based upon 1999 FERC Form-1 data, B.L. England operated at a 39% capacity factor, higher than Indian River (33%) and Indian River and Vienna combined (28%). Mr. Chernick asserted that, according to Schedule NRG-4, NRG assumed that Indian River would operate at a 71.7% capacity factor, but that it has been operating at half that capacity factor, and that operating costs are also higher than assumed by NRG. Mr. Chernick asserted that, on November 29, 2001 NRG announced the purchase of four coal plants, including some small combustion turbines, from FirstEnergy.[13] Mr. Chernick asserted that the sale consists of 14 coal units, of which 13 units, on average, have a capacity of 143 mW, compared to B.L. England's coal units' average of about 142 mW. Mr. Chernick asserted that the average price for the FirstEnergy coal units is estimated to be $519/kW, about 3.4 times the price of B.L. England. Mr. Chernick asserted that, even discounting the lesser value of the oil-fired Unit 3 at B.L. England, the facility's value is $178 million, two and one-half times the $68.5 million price offered by NRG, which Mr. Chernick asserted to be understated by $100 million or more.

Mr. Chernick concluded his testimony by asserting that a re-auction of generation assets could produce higher prices. Mr. Chernick asserted that, there were two instances where utility-owned nuclear facilities were re-auctioned at higher prices, and another two instances where non-utility owned facilities were purchased and resold at higher prices.

Supplemental Comments and Reply Comments

Pursuant to the schedule established by the Board, both ACE and the Advocate submitted supplemental comments and supplemental reply comments. The comments are summarized briefly below.

[13] "NRG Energy to Acquire 2,535 MW of Ohio-Based Generation from FirstEnergy." Press release of NRG, dated November 30, 2001.

Company Supplemental Comments

In its supplemental comments, ACE asserts that the supplemental testimony filed on behalf of itself and NRG reinforces the facts established in the initial public/legislative-type hearing and shows that the sale price of the Fossil Assets reflect fair market value of the units.

ACE asserts that the sale of Deepwater to NRG will not result in any stranded cost responsibility for the Company's customers, and that the sale of Deepwater is consistent with the Final Order. The Company asserts that the Final Order allowed Deepwater to be transferred to an affiliate, and determined that the Company's customers would not be responsible any stranded costs associated with the facility. The Company also asserts that the Final Order provided that, in the event Deepwater is sold by the affiliate to a non-affiliate during the four-year transition period, the net after-tax gain over the adjusted book value of Deepwater would be shared equally between the Company and its customers. The Company asserts that, prior to the issuance of the Final Order, Conectiv decided that Deepwater did not fit the affiliate's strategy of focusing primarily on combustion turbine combined-cycle technology and that a decision was made that Deepwater would be included in the sale of the Fossil Assets. The Company asserts that it decided not to transfer Deepwater to an affiliate and then sell it to NRG since Conectiv had already agreed to sell the facility to NRG. The Company asserts that a transfer and subsequent sale would have necessitated additional and unnecessary regulatory and accounting activities and would not have provided any economic benefit to customer, and that selling the facility directly to NRG would not have any impact on customers or stranded costs.

ACE asserts that the sale price of the Fossil Assets still represents the fair market value of the Fossil Assets. The Company asserts that events that have transpired since the date of the original agreements, as well as the date of the original hearing in this matter, that support the reasonableness of the sale price. The Company argues that the Advocate's witness acknowledges that the sale of Deepwater to NRG will not affect stranded costs, and that the sale price allocation for ACE's interest in Conemaugh and Keystone provides a result which is consistent with the sale price of capacity for similar facilities.

ACE asserts that the only contested issue is with respect to the valuation concerns relating to B.L. England. ACE asserts that Units 1 and 2 of B.L. England, representing 63% of the facility's generation capacity, utilize a coal-fired cyclone boiler technology that was developed to use a relatively low quality, high ash and high sulfur coal. The Company asserts that the coal units are smaller and have higher heat rates, higher operating costs, and higher NOx and SO2 emissions than other generation facilities and, therefore, have an impact on the relative value of the facility. The Company asserts that it has experienced recent permitting problems with the DEP and is currently testing the viability of burning more expensive, lower sulfur coal in Unit 1 of B.L. England in an attempt to finalize a new operating permit to allowed continued operation of the unit. In addition, ACE asserts that another potential environmental issue exists involving an investigation by the EPA to evaluate the facility's compliance with "new source review" federal rules.

The Company asserts that it has provided uncontroverted factual testimony concerning recent developments at B.L. England with respect to fuel use, permitting and environmental issues, all of which suggest that the value of B.L. England is, if anything, less than when it was valued at the time of the original agreements.

Advocate Supplemental Comments

In its supplemental initial comments, the Advocate continues to oppose the sale of B.L. England to NRG as currently structured.

The Advocate asserts that the proposed sale price of B.L. England is unreasonable since it is far lower, on a per-kilowatt basis, than comparable units in the sale of Delmarva's fossil assets to NRG. The Advocate asserts that the difference in sale prices for other Conectiv assets and B.L. England cannot be explained by disparities in plant performance.

The Advocate asserts that ACE has not provided any substantial evidence to refute the Advocate's sale price findings. The Advocate asserts that, contrary to the assertions of ACE's and NRG's witnesses, a higher sale price for B.L. England is not unreasonable, as current sale prices have not declined since the time of the Company's auction. The Advocate asserts that the Company's analysis of the difference between spot electricity prices and spot fuel prices (the so called "spark spread") as being a key indicator of potential gross profit margins and, in turn, the value of generation facilities, is fundamentally flawed.

Finally, the Advocate asserts that ACE's assertion that re-auctioned assets are inherently viewed as "damaged goods" and would not yield a higher price is unsupported. The Advocate provides examples of various nuclear and fossil facilities that were successfully re-auctioned, or were purchased and resold, for higher prices.

Company Supplemental Reply Comments

ACE provided supplemental reply comments responding to the arguments made by the Advocate, and reiterating its prior arguments.

ACE asserts that the Advocate incorrectly argues that B.L. England has a comparable value to other facilities, based on faulty assumptions made by the Advocate's witness. The Company asserts that the record in this proceeding contains detailed information concerning the manner in which each of the Fossil Assets was valued by NRG. The Company asserts that B.L. England is "comparable" to Indian River only if Indian River's production cost, which is two-thirds the production cost of B.L. England, Indian River's higher output and B.L. England's cyclone boiler technology, is ignored. ACE also notes that, even though NRG utilized the same basic valuation methodology for all of the Fossil Assets, the Advocate only has concerns with respect to B.L. England.

ACE asserts that there is no factual basis for the Advocate's argument that B.L. England should be compared to other facilities that NRG recently agreed to purchase from another utility. The Company asserts that NRG's witness' testimony and exhibits shows that the other facilities use lower priced fuel and have lower operating costs due to their proximity to each other. The Company asserts that the Advocate has not provided any credible support for its assertion that there should be a higher market value for B.L. England. The Company maintains that the prices of individual units can vary greatly from an overall price for a package of assets, and that the individual factors associated with a particular unit must be considered when valuing packages of units. ACE asserts that the Advocate disregards the cyclone boiler technology issue with respect to valuation. The Company asserts that the extensive testimony in the record dealing with the concerns of this technology cannot be ignored.

ACE asserts that there is no reasonable basis to conclude that a re-auction of B.L. England would produce a higher market value. The Company asserts that the Advocate's argument is based on an unsupported comparison of B.L. England to dissimilar situations regarding subsequent sales of facilities. The Company asserts that the Advocate ignores other critical factors, such as B.L. England's smaller capacity, higher operating and capital costs, relatively high heat rate and higher NOx output due to the cyclone boiler technology. The Company asserts that even higher operating costs are likely due to the potential for the DEP to require the use of lower-sulfur coal. The Company asserts that the Advocate did not dispute the demonstrated higher price for this type of coal, a factor the Company maintains has an undisputable effect on overall value of a facility, nor did it dispute other industry and economic factors impacting the current market for generation facilities.

The Company asserts that the Advocate's own witness admitted that B.L. England's compliance with DEP directives to reduce emissions and to utilize lower sulfur coal would also result in increased costs that would have to be considered in any assessment of the market value of the facility. The Company asserts that the Advocate fails to acknowledge these factors in arguing that a re-auction could produce a higher sale price. The Company asserts that the fact that greater value could possibly be obtained for a nuclear facility does not provide any basis to conclude that greater value could be achieved for a coal facility.

Advocate Supplemental Reply Comments

In its supplemental reply comments, the Advocate reiterated its prior arguments and argued that ACE has presented nothing that substantially refutes the Advocate's supplemental comments.

The Advocate asserts that neither ACE nor NRG have conclusively demonstrated that the potential additional costs attributable to compliance with environmental requirements at B.L. England will, in fact, be incurred. The Advocate notes that DEP-required test burns of lower sulfur coal are still in progress and asserts that no conclusions should be drawn at this time as to what the DEP may ultimately require at B.L. England. The Advocate asserts that, even if the use of lower sulfur coal is required as a permanent solution, the estimates for the cost of such coal are unsupported by any data. The Advocate notes that the EPA's new source review process and the DEP's NOx controls permitting process are also still ongoing, and submits that it is premature to speculate about what added costs, if any, may result from any EPA or DEP action.

The Advocate also asserts that potential remediation costs, cited by ACE to have an effect on the sale price, are not material relative to the total asset sale price. The Advocate asserts that the environmental concerns raised by ACE's and NRG's witnesses are speculative and do not provide convincing support for a lower sale price for B. L. England.

The Advocate asserts that notwithstanding ACE's arguments regarding the value of B.L. England, the fact remains that the sale price of the facility is low in comparison to other recent fossil and coal facility sales. The Advocate asserts that the differences in sale price for Indian River and Vienna could not be explained by plant performance, as these facilities had lower capacity factors than B.L. England. The Advocate therefore asserts that its witness provided ample support of his claim that Indian River, Vienna and similar unbundled units being sold to NRG by FirstEnergy do not appear to be more valuable than B.L. England.

The Advocate asserts that NRG's valuation methodology of the Fossil Assets did not include any basis for assumptions and values used in NRG's analysis, while the Advocate's witness based his analysis on other recent similar sales. The Advocate asserts that, based on a comparison of these sales, its witness did not find the sale price of Keystone and Conemaugh to be unreasonable, whereas the sale price of B.L. England was far lower.

NRG Comments

NRG asserts that the Advocate's supplemental comments are a reiteration of the Advocate's pre-filed testimony, and do not take into account information provided by NRG during discovery or the testimony and exhibits introduced by NRG at the evidentiary hearing. NRG asserts that the evidence provided decisively refutes the Advocate's assertion that B.L. England is of comparable value to Indian River or to other coal facilities that NRG recently agreed to purchase from another utility. NRG notes that the Advocate's witness does not object to the sale price of Conemaugh, Keystone and Deepwater. NRG asserts that B.L. England differs from Indian River and the other coal facilities, and that B.L. England's operating costs are significantly higher than these other facilities. NRG asserts that, when it conducted its market value analysis in 1999, environmental restrictions for B.L. England made the facility less profitable and, therefore, less valuable than Indian River. NRG asserts that stricter environmental constraints and higher operating costs at B.L. England have since made the facility less valuable and that, if B.L. England were to be re-auctioned, NRG would not bid for the facility. NRG lastly asserts that, on cross-examination, the Advocate's witness conceded that the environmental restrictions on B.L. England make the facility less valuable.

Discussion and Findings

The Board has carefully reviewed the record developed in this matter. The Board notes that this Order is limited to the following aspects of the Company's filing relating to the sale of its interest in its Fossil Assets, specifically: (1) whether the proposed sale of the Company's Fossil Assets is consistent with the Board's Auction Standards Order; (2) whether the Company has met the requirements set forth in N.J.S.A. 48:3-59; (3) the amount of the Company's eligible stranded costs associated with sale of the Fossil Assets as defined by N.J.S.A. 48:3-51; (4) whether the Company may recover such eligible stranded costs pursuant to N.J.S.A. 48:3-61(a)(1); and (5) whether the Fossil Assets qualify as eligible facilities under Section 32 of PUHCA. ACE also seeks a finding by the Board, pursuant to N.J.S.A. 48:3-62(c)(1), that the full amount of eligible stranded costs either may constitute, or be included as part of, the principal amount of transition bonds for which the Company may seek approval to issue under the Act. With regard to the request concerning transition bonds, the Board, in its July 21, 2000 Order, in Docket No. EM99110870, stated that it would reserve decision regarding the amount, if any, of stranded costs eligible for securitization until a later date after the Company's sale of its fossil assets has been evaluated and considered by the Board. As described below, this Order does not address this issue. In addition, this Order addresses issues raised in both the public/legislative-type hearing and the supplemental evidentiary hearing, and the written comments including, among other things, whether the process for the selection of NRG as the winning bidder was reasonable, whether the sale reflects the full market value of the assets, and whether the Board should authorize the sale of Deepwater to NRG.

Based on the Board's review of the requirements of the Act, the procedures which have been followed and the record which has been developed in this matter, the Board is convinced that a thorough record has been developed and that the parties have had an opportunity through

discovery, public/legislative hearing, including the opportunity to present testimony, comments and reply comments to the Board, to review and explore the underlying facts regarding the Company's proposal, and to present their factual, policy and legal concerns to the Board regarding the proposed sale, and other related issues of concern. See, I/M/O Public Service Electric and Gas Company's Rate Unbundling, Stranded Costs, and Restructuring Filing, 330 N.J. Super. 65, 117-120 (App. Div. 2000), affirmed, 167 N.J. 337 (2001).

Regarding the Advocate's assertions that an evidentiary hearing is necessary, the Board subsequently determined to reopen the record and to conduct an evidentiary hearing to review whether the proposed sale price of the Fossil Assets reflects the current market price of the assets. Both the Company and the Advocate had an opportunity to present testimony, propound discovery and cross-examine witnesses. Board Staff also participated in the cross-examination of witnesses. It is the opinion of the Board that said hearing renders moot the Advocate's contention regarding the need for an evidentiary hearing, as all parties have been provided a full opportunity to address all areas of concern related to the Company's petition, including the proposed sale price of the Fossil Assets.

During its review of this matter, the Board learned that ACE did not transfer Deepwater to an affiliate, as it was authorized to do in the Board's Summary Order and, subsequently, in the Final Order. Indeed, the Company's petition acknowledged the provision in the Summary Order authorizing the transfer of Deepwater and the foregoing of recovery of any stranded costs associated with the facility, yet was silent as to the status of the transfer process. As discussed above, the Board reopened the record in this matter for additional proceedings to, among other things, provide the Company an opportunity to explain why it was proposing to directly sell its interest in Deepwater to NRG rather than first transferring the facility to an affiliate, as authorized, and to supplement the record to enable the Board to determine whether the proposed sale to NRG should be approved by the Board. The Company's explanation through its supplemental testimony and supplemental comments in this matter notwithstanding, the Board FINDS that ACE should either have: (1) completed the transfer of Deepwater to its affiliate, pursuant to the Summary Order and the Final Order, prior to agreeing to sell the facility to NRG; or (2) requested the Board's approval of the sale at the time the Company filed its petition in this matter, pursuant to N.J.S.A. 48:3-7. Since the transfer did not occur, for whatever reason, and even though Deepwater's costs are recorded "below the line" and, for ratemaking purposes, are not eligible for stranded cost recovery, the facility still remains utility property and any proposed divestiture thereof requires Board approval. Therefore, the Board will review the proposed sale of Deepwater to NRG in a manner consistent with its consideration of the proposed sale of the other facilities comprising the Fossil Assets.

Standards for Review for Approval of the Sale

As a preliminary matter, the Board has considered what review criteria should be used in assessing the appropriateness and reasonableness of the sale of the Company's interest in its Fossil Assets. The Board FINDS that N.J.S.A 48:3-59(b) requires that, prior to the commencement by an electric public utility of the solicitation of bids for the sale of generation assets subject to recovery pursuant to N.J.S.A. 48:3-61 and N.J.S.A. 48:3-62, the Board shall establish standards for the conduct of such a sale by the utility. N.J.S.A. 48:3-59(b) indicates that such standards shall include provisions for the Board to monitor the progress of the bid process to ensure that the process is conducted by parties acting in their best interest and in a manner designed to ensure a fair market value determination and does not unreasonably preclude participation by prospective purchasers. N.J.S.A. 48:3-59(b) further requires that the

standards adopted by the Board include provisions that the purchasing entity shall: (1) recognize the existing employees bargaining unit, and shall continue to honor and abide by an existing collective bargaining agreement for the duration of the agreement. The new entity shall be required to bargain in good faith with the existing collective bargaining unit when the existing collective bargaining agreement has expired; (2) hire its initial employee complement from qualified employees of the electric public utility employed at the generation facility at the time of the functional separation or divestiture; and (3) continue such terms and conditions of employment of employees as are in existence at the generation facility at the time of the functional separation or divestiture.

The provisions of N.J.S.A. 48:3-59(c) require that, prior to completing the sale of generation assets subject to recovery pursuant to N.J.S.A. 48:3-61 and N.J.S.A. 48:3-62, an electric public utility shall file for, and obtain approval of, the sale by the Board. The Board shall approve such filing subject to the provisions of N.J.S.A. 48:3-59(d) if it finds: (1) the sale reflects the full market value of the assets; (2) the sale is otherwise in the best interest of the electric public utility's customers; (3) the sale will not jeopardize the electric power system; (4) the sale will not result in undue market control by the prospective buyer; (5) the impacts of the sale on the utility's workers have been reasonably mitigated; (6) the sale is consistent with standards established by the Board in N.J.S.A. 48:3-59(b); (7) the sale includes provisions that the purchasing entity shall recognize the existing employee bargaining unit and shall honor and abide by any existing collective bargaining agreement for the duration of the agreement; (8) the sale of the generation assets includes a provision that the purchasing entity shall hire its initial employee complement from among the employees who are employed at the generation facility at the time of the sale; and (9) the sale of the generation assets includes a provision that the purchasing entity shall continue such terms and conditions of employment of employees as are in existence at the generation facility at the time of the sale.

Compliance with Auction Standards

The Board's review of the record for compliance with the Auction Standards Order indicates the following observations as set forth below.

Auction Standard 1. The auction process must be designed to foster competition among bidders, ensure maximum sales price, thereby minimizing stranded costs, and encourage bidder flexibility. The process must be designed in a way to maintain necessary confidentiality in order to restrict the possibility of gaming and to maintain an optimal situation for the development of a comprehensive energy supply market for competition. The process must also consider the costs incurred. The auction should be structured to maximize the sale price while reasonably managing costs, administrative and otherwise. The auction process should permit sufficient flexibility so that bidders may bid on a number of generation site combinations, unless ACE can demonstrate justification for a packaged bidding structure for certain plants. Any grouping of assets for sale should balance such considerations as market demand from prospective buyers, asset characteristics, projected price, stranded costs considerations, and market power issues. In the case where packaging is permitted, bidders must still have had the ability to bid on any individual generation site or sites.

The Company utilized a multi-step process to identify and reach potential bidders for the sale of its interest in its Fossil Assets. The purpose of the multi-step process was to market the assets widely in order to maximize the purchase price. Additionally, by contacting a large number of prospective bidders, the Company attempted to facilitate the development of a competitive

energy supply market by inviting bids from a diverse group of potential bidders. In May 1999, early interest letters were sent to approximately 1,200 companies indicating the Company's intention to sell its interest in its fossil and nuclear generation assets. In response to the early interest letters, 76 interested parties provided formal expressions of interest in acquiring the Company's interest in the Fossil Assets. The Company, in an effort to maintain necessary confidentiality, then required that the prospective bidders execute a confidentiality agreement. Forty-one parties were willing to do so, and were determined to be qualified bidders by the Company. Detailed offering memoranda were sent to the 41 parties on July 19, 1999. Fourteen parties submitted indicative bids. The Company, upon reviewing the indicative bids, reduced the number of qualified bidders to ten, based upon price, financial strength, experience and exceptions to the terms of the sale. Upon the completion of due diligence efforts by the ten parties, the Company provided final bid instructions and draft transaction documents to the ten parties. On December 8, 1999, the Company received five final bids. The Company subsequently entered into negotiations with the highest bidder but was unable to successfully negotiate terms, including the retention by ACE of certain environmental liabilities that were acceptable to the Company and consistent with the Auction Standards Order. As a result of the impasse with the first bidder, the Company began negotiations with the second highest bidder, NRG. During the negotiations, NRG submitted an improved final bid, narrowing the difference between NRG's bid and the highest bid. As a result of its analysis of the improved NRG bid, and an evaluation of the prices, terms and conditions of other recent fossil assets sales, the Company determined to accept NRG's offer.

Auction Standard 2. Bidder qualifications should be reasonable and not unduly restrictive. Qualifications may include such criteria as: financial capability; regulatory or other legal requirements; experience in ownership and/or operation of electric generation facilities; labor and industrial relations experience; and relevant environmental and community involvement track records. Prospective bidders must be required to indicate the intended use of the facilities.

From May through July 1999, Confidentiality Agreements and Requests for Qualifications ("RFQ") were issued to all prospective bidders who expressed interest in the Fossil Assets. The RFQ solicited financial, operating and technical information to demonstrate that prospective buyers were both financially capable of entering into a transaction with the Company and likely to satisfy regulatory requirements. Interested parties who executed the Confidentiality Agreement and satisfied the RFQ were eligible to participate further in the auction process.

Auction Standard 3. Any "short list" or final bidding group must include enough participants to provide assurance that there is sufficient competition for any particular bundle or individual plant. The Board recognizes that some of ACE's generation facilities are jointly owned. The Board further recognizes that any transaction involving those jointly owned facilities must be both consistent with the joint ownership agreements and with the existing contractual rights of the joint owners, and must also consider environmental and other issues.

As noted under the first Auction Standard, the Company made substantial efforts to promote competition and create interest in the sale of the Fossil Assets. In the early stages of the bid process, the Company's interest in the Fossil Assets was unbundled into separate facilities. After reviewing bidder preferences, the Company's interests were bundled into wholly owned and jointly owned facilities to maximize the value in the final bid stage. The final bids provided sufficient competition for the bundled facilities, either wholly owned, jointly owned, or both.

Auction Standard 4. ACE must ensure that access to all relevant information is provided to all prospective bidders (this may include, but will not necessarily be limited to: plant and site data; transmission and fuel supply infrastructure; interim buyback requirements, if any; State and federal regulatory requirements; relevant market information, environmental and other liabilities; labor responsibilities; industry and market analysis; and treatment of emission credits). Bidders should be provided with appropriate access to relevant documentation and key personnel to perform necessary due diligence investigations. The bidders should also be informed about regulatory and commercial terms of sale in order to make informed decisions and correctly analyze the value of the assets being offered.

An Offering Memorandum and virtual data room on CD-ROM were issued to Qualified Bidders. The Offering Memorandum provided information regarding the Fossil Assets, the PJM marketplace, and the terms of sale anticipated by the Company. The virtual data room provided detailed technical and operating information about the assets. Technical and management meetings with the Company were held, as well as physical site tours. Qualified Bidders were also given the opportunity to pose questions relevant to their evaluation of the assets.

Auction Standard 5. ACE, upon completion of the auction, and as part of its request for approval, will be required to submit a market power analysis for regulatory review. ACE must demonstrate that the sale of any generation facility will not create or enhance market power in the relevant market, and should take into account the effect of any identified load pockets. The Board will give particular attention to any buyer which currently owns or controls electric generation assets in the State of New Jersey.

The Company's non-operating minority interest in the jointly owned Conemaugh and Keystone facilities is small and, therefore, the market power of NRG or the co-owners will not be altered significantly by the transaction. While a greater potential for market power could conceivably exist for the Company's wholly owned B.L. England and Deepwater facilities, NRG is a relatively new entrant into the PJM market and will not be in a position to combine existing generation resources with the purchase of ACE's interest in the Fossil Assets to pose any market power concerns.

Auction Standard 6. ACE must demonstrate that it has adequately provided for system reliability and the provision of safe, adequate, and reliable service post-divestiture. ACE must demonstrate that there will be an entity or structure in place for it to meet the reasonably anticipated load requirements (including basic generation service) through retail phase-in, and provide local area support, if necessary. Buyers must be required to become a member of the local control area independent system operator entity and meet all applicable operational and reliability standards.

Pursuant to the Stipulation of Settlement regarding the Company's Unbundling, Stranded Costs, and Restructuring filings, the elements of which were approved with modifications in the Summary Order dated July 15, 1999, and in the Final Order dated March 30, 2001, the Company agreed to conduct a competitive procurement process to meet the Company's BGS obligation. The Company filed a petition[14] with the Board on March 14, 2000, several months later than contemplated in the Summary Order, requesting approval of a bidding process for

[14] In The Matter of the Petition of Atlantic City Electric Company For Approval of a Request For Proposals, Authorization of a Competitive Procurement and To Enter Into a Contract For Basic Generation Service Supply, Docket No. EM00030156.

energy and capacity for the purposes of satisfying a portion of its BGS requirements. The petition included a request for approval of a 350 mW bid to replace energy and capacity associated with the Company's interest in the nuclear assets. The Company filed two subsequent petitions requesting approval of two additional bidding processes for energy and capacity, on August 30, 2000 for 300 mW of capacity and energy, and on March 9, 2001 for 400 mW of capacity and 300 mW of energy. In addition, the Company had entered into a PPA for BGS supply with NRG for the purchase by ACE of 400 mW of unforced capacity and firm energy from NRG for the period commencing on the closing on the sale through August 31, 2002.[15] Lastly, NRG must, and has agreed to, comply with all PJM requirements, including all applicable operational and reliability standards. In addition to the foregoing, the Board, in its Decision and Order dated December 11, 2001, in Docket No. EX01050303, approved an auction process for ACE and the other New Jersey electric utilities for the provision of BGS for the fourth year of the transition period to retail competition in New Jersey, pursuant to N.J.S.A. 48:3-57. If the Board certifies the auction results as required in its Order, ACE's BGS requirements will be provided by the successful bidder(s) for the period beginning August 1, 2002 through July 31, 2003.[16]

Auction Standard 7. Absent a showing by ACE that retention of such liabilities provides a substantial risk-adjusted benefit to customers, all on-site environmental liabilities associated with the auctioned property shall be assumed by the purchaser unless otherwise required by applicable local, State, and federal laws. The buyer(s) shall comply with all environmental standards as embodied in existing State and federal statutes and regulations and associated permits, and as subsequently modified through legislative or regulatory actions.

Under the PSAs entered into between the Company and NRG, NRG has agreed to assume all pre-closing on-site environmental liabilities associated with the Fossil Assets. NRG will also assume all post-closing on-site and off-site environmental liabilities associated with the Fossil Assets. NRG will also comply with all applicable State and federal environmental laws and regulations. As noted above, there recently were, and continue to be, certain potential environmental liabilities concerning Unit 1 of B.L. England that were disclosed during the proceedings in this matter. These liabilities will also be assumed by NRG.

Auction Standard 8. All bidders on the short list, or in the final bidding group, shall be required to submit to ACE, on a confidential basis, a disclosure of all formal notices of violation of local, State, and federal environmental permits applicable to the ownership or operation of electric generation facilities for the past five year period. The environmental performance record for the proposed buyer(s) shall be submitted and made public as part of the petition by ACE for approval of the sale.

When ACE issued its RFQ to all prospective bidders who expressed interest in the Fossil Assets, the Company required the bidders to provide information regarding their environmental management and community involvement. NRG provided information regarding its environmental performance record.

Auction Standard 9. The divestiture petition must include a reasonable transition plan, plus a system of reporting such plans, for the incumbent generation workforce, including, but not

[15] As noted in the procedural history, this last PPA was subsequently terminated by ACE and NRG.

[16] By Order dated February 15, 2002, the Board certified the final results of the BGS auction. Thus, ACE's BGS requirements for the period beginning August 1, 2002 through July 31, 2003 will now be met by suppliers other than the Company.

limited to, assurances that existing pension and other post-retirement benefits and entitlements accrued through the date of sale are protected, and requirements that the buyer assume any existing collective bargaining agreements associated with these facilities. In addition, ACE is expected to assist employees (both union and non-union) in obtaining positions with the buyer(s).

The Company is a minority, non-operating owner of each of the jointly-owned generation assets. As a minority owner, pursuant to the terms of the co-owners' agreement, it contributes to employee salaries and benefits. Conectiv employs none of the employees at the facilities, either union or non-union. Instead, the respective operators of the facilities employ all of the workers at each of the generation facilities where the Company is a minority owner, and all responsibility for employee issues rests with the facility operators. Therefore, since Conectiv does not employ any of the workers at Keystone and Conemaugh, and since the operators of these facilities will remain unchanged as a result of the proposed sale, the sale itself will not alter the status of any ACE employees, making an employee transition plan unnecessary. With regard to ACE's wholly owned generation facility, the Company does employ the union and non-union employees at these facilities. NRG has agreed to retain all bargaining unit employees, as well as most management employees, at the facility. The Company expects fewer than ten management employees will be terminated as a result of the sale. Any employee terminated as a result of the sale will be offered a competitive severance package. Bonuses will be provided to management employees who transfer to NRG.

Auction Standard 10. Upon completion of the auction process, and with its petition for approval of the sale, ACE shall be required to submit a complete and accurate summary of the auction proceedings and outcome. ACE must be prepared to provide to the Board in writing the rationale behind the exclusion of any bidder at each stage of the auction process.

The Company presented a summary of the auction and sale proceedings in its testimony at the public/legislative-type hearing on June 22, 2000 and in its subsequent written comments. Taken together with the Company's responses to data requests propounded by Board Staff and the Advocate, the Company's submission appears to constitute a complete and accurate summary of the auction and sale proceeding.

The Board notes that, in the Advocate's comments concerning the Company's compliance with the Auction Standards Order, the Advocate argues that the Company did not satisfy the Board's Auction Standards, asserting that the Company did not complete the competitive bid process and instead prematurely aborted the auction process in order to enter into sales negotiations with NRG. The Advocate asserts that the Company's actions during the auction process ignored another important point, that being that the Company was under no obligation to sell its Fossil Assets to any party if the price was too low. ACE argues that it has complied with all of the Auction Standards set out by the Board for the sale of the Company's Fossil Assets. The Company argues that it accepted NRG's offer, which it determined to be reflective of the current market price for such assets.

The Board agrees with the Advocate that the Company has an obligation to maximize, to the best of its ability, the market price of its interest in the Fossil Assets in order to minimize its stranded costs. Both the Company and the Advocate have provided significant testimony and comments concerning the appropriateness of the sale price of the Fossil Assets, with particular emphasis on the valuation of B.L. England. There appears to be no disagreement with regard to the valuation of Conemaugh, Keystone and Deepwater which, together with certain other

generation-related assets, comprise the balance of the Fossil Assets. The primary point of contention in this proceeding has been whether B.L. England's sale price is representative of the market value of this particular type of generation facility.

The Advocate raises an argument concerning the Company's cessation of negotiations with the highest bidder and the subsequent successful negotiations with NRG, the second highest bidder. The Advocate maintains that ACE did not maximize the sale price for B.L. England and, therefore, did not obtain the market value for the facility, as required by Auction Standard No. 1. While the Company had an obligation to reasonably comply with all requirements set forth in the Auction Standards Order, the Company has provided convincing arguments that continued negotiations with the highest bidder would likely have required the Company to assume certain environmental liabilities that would have significantly and adversely impacted the Company's ability to comply with the requirements set forth in Auction Standard No. 7. The Board FINDS that ACE's decision to negotiate a successful sale with NRG after its unsuccessful attempt to negotiate a sale with the highest bidder does not violate the Auction Standards Order. Indeed, the Company's efforts resulted in two PSAs that provide for NRG to assume all pre-closing on-site, and all post-closing on-site and off-site, environmental responsibilities associated with the Fossil Assets while, at the same time, obtaining an improved final bid from NRG, thereby narrowing the difference between NRG's bid and the highest bid. Therefore, the Board FINDS that the Company has satisfactorily demonstrated substantial compliance with the Auction Standards Order for all facilities comprising the Fossil Assets.

The Board FINDS that, with the above-noted Board determination to include the proposed sale of Deepwater as part of ACE's requests in this matter, the requirement that the proposed sale of ACE's interest in its Fossil Assets be submitted to the Board for its review and approval has been met. Therefore, in light of the Board's findings, the Board HEREBY WAIVES the advertising requirements as set forth in N.J.A.C. 14:1-5.6(b), as the Board has determined that the Company has complied with the aforementioned Auction Standards Order for all its facilities, including Deepwater..

As noted above, the Company agreed to a purchase price of approximately $178.4 million and subject to certain adjustments at closing, for the Fossil Assets. The Advocate, in its initial comments, argues that the Company has contracted to sell its interest in its Fossil Assets at a price that was not allocated among the various generation facilities and that the market price of each facility was not ascertained through the bid process but, rather, after the fact by NRG. The Advocate argues that the allocation of the sale price to the various plants is a critical issue, since the allocation ultimately impacts the resulting stranded costs subject to recovery from the Company's customers. The Advocate therefore argues that the sale either should be rejected as not being in the public interest or, alternatively, that the Board should adjust the allocation of the sale proceeds to B.L. England for ratemaking purposes.

The Board, to some extent, shares the Advocate's concern regarding the allocation of the sale proceeds, and that the allocation creates significant stranded costs for B.L. England, as the sale price of $68.5 million for B.L. England falls below the approximate book value of $227.5 million as of December 31, 1999. However, the sale price for ACE's interest in Conemaugh and Keystone is $96.1 million versus an approximate book value of $34.5 million as of December 31, 1999, providing a gain on these facilities for the Company's customers. Combined, the proposed sale of the Fossil Assets would result in net stranded costs to customers of $97.4 million, regardless of how the sale proceeds were allocated among ACE's Fossil Assets. Moreover, as described herein, ACE and NRG have submitted credible evidence in the record

to explain why a lower value was assigned to B.L. England. The Advocate's argument that the Board should adjust the allocation of the overall Conectiv proceeds to increase the valuation of B.L. England for ratemaking purposes is, on its face, contrary to the Advocate's, and the Board's, longstanding support for divestiture as being the preferred method for determining market value and stranded costs of generation assets.

In its Final Order, the Board authorized ACE to transfer Deepwater at the book value of the facility. The Board also found in its Final Order that, in the event Deepwater was sold to a non-affiliate prior to August 1, 2003, any gain on the sale would be shared equally between the Company's customers and its shareholders. The proposed sale price is approximately $13.8 million, of which $12.1 million was allocated to the Deepwater facility and certain emissions allowances and Merrill Creek interests, while $1.7 million was allocated to excess NOx and SO2 emission allowances associated with the facility. While it is not anticipated that there will be any gain associated with the sale of Deepwater, the Board reserves its right to review the accounting treatment associated with the transfer and sale of Deepwater to ensure that the rights of ACE's customers are fully preserved. Moreover, under no circumstance will any stranded costs associated with Deepwater be recoverable from customers

Certain confidential information provided by ACE during discovery and in its testimony in this proceeding, and presented by the Advocate in its initial comments, indicated that the sale price of B.L. England, on a sale price per-kilowatt basis, appeared to compare unfavorably to certain other fossil and coal generation facilities that have been sold in the United States and within the PJM region. The Board was not satisfied that sufficient information was presented by the Company to support the reasonableness of the sale price. The Board subsequently determined that a supplemental evidentiary proceeding was appropriate to further explore the valuation placed by NRG on B.L. England. The Board reopened the record to, among other things, provide the parties an opportunity to provide supplemental testimony and to cross-examine witnesses in an effort to update the record to compare the valuation of the Fossil Assets to current market prices.

The supplemental testimony presented by the Company, NRG and the Advocate served to update and further develop the record regarding the valuation of B.L. England. As described above, the parties, through their witnesses, provided extensive evidence regarding the valuation of the facility. In reviewing the record it is apparent that B.L. England possesses certain physical and operational characteristics that may make the facility less desirable to a prospective buyer. The Board is comfortable that the best test of a facility's value is the price that a buyer is willing to pay for that facility through a competitive divestiture process. The Board recognizes that, over time, the value of the B.L. England may rise or fall as the result of changing market conditions and changing environmental requirements, and based on the evidence presented, the Board is of the view that there is no certainty that re-bidding B.L. England would yield a higher sale price at this time. In addition, despite the Advocate's arguments to the contrary, based on its review of the supplemental testimony, the Board is persuaded that there is an increased likelihood that B.L. England's current environmental situation will result in higher operating costs over its useful life, whether the facility remains under the Company's ownership or is sold to NRG. Based on the evidence presented, the Board does not believe that a re-bidding of B.L. England at this time would yield a significantly higher price and, in fact, a re-bid could well yield a lower price. Thus, in the Board's view, a re-bid would not be a prudent regulatory action.

Based on the foregoing, the Board CONCLUDES that the record in this proceeding adequately demonstrates that the proposed sale price of the Company's interest in its Fossil Assets reflects the full current market value of the assets, and that the record adequately demonstrates that the sale is in the best interest of the Company's customers, pursuant to N.J.S.A. 48:3-59(c). The Board therefore FINDS that the provisions of N.J.S.A. 48:3-59(c) have been met in their entirety. Therefore, the sale of the Company's interest in its Fossil Assets for approximately $178.4 million to NRG is HEREBY APPROVED.

The Board, in approving the sale of the Company's interest in its Fossil Assets, reserves judgment with regards to making a final determination with respect to the net divestiture proceeds, including the Company's treatment of the federal income tax benefits associated with the divested assets. The Board DIRECTS the Company to: 1) file with the Board within 15 days of the closing date of the asset sale proof of closing and the net transaction cost; and 2) subsequently, the Company shall advise the Board upon receipt by the Company of a private letter ruling from the IRS regarding the treatment of the federal income tax benefits associated with the divested assets, and the Company shall, within 30 days of receipt of such a ruling, make a compliance filing with the Board which shall include a final proposed determination of the net divestiture proceeds, based upon actual results of the closing of the asset sale.

Having reviewed the record in this matter as it relates to the quantification and recoverability of eligible stranded costs associated with the approved sale of ACE's Fossil Assets, the Board FINDS that the starting point for consideration should be the Company's summary of eligible stranded costs, as estimated in Exhibit C - Update No. 1, on a net-of-tax basis, of approximately $105.0 million as of April 30, 2000. This estimate will be subject to the adjustment described below. This estimate shall be further adjusted at closing to reflect actual data at the time of closing, and the actual amount shall be provided to the Board and the Advocate subsequent thereto.

With regard to ACE's proposed stranded cost recovery of loss on reacquired debt in an approximate amount of $4.1 million, consistent with the Board's prior Order in Docket No. EM99110870, the Board believes that it is inappropriate for the Company to recover this item as a stranded cost. The Board FINDS that such costs do not fall within EDECA's definitions of stranded costs or bondable stranded costs, as set forth in N.J.S.A. 48:3-51. Thus, this amount should be subtracted from the aforementioned $105.0 million estimate. Therefore, the Board FINDS that losses on reacquired debt do not meet the criteria for stranded cost recovery under EDECA. To the extent these costs have not been reflected in current rates, ACE may seek recovery of such unamortized costs in its next base rate proceeding, at which time all of the Company's costs and revenue will be evaluated by the Board. At that time, the issue of any double recovery can be more fully explored. The Company can continue to defer such unamortized losses until the Board makes a decision in the Company's next base rate case.

As a result of the above adjustment to ACE's proposed level of eligible stranded cost recovery associated with the sale of the Fossil Assets, the Board HEREBY DETERMINES the amount of stranded costs, eligible for recovery by the Company, as defined by N.J.S.A. 48:3-51, to be approximately $100.9 million as of April 30, 2000, subject to further adjustment at the time of closing and subsequent verification to reflect actual data at the time of closing. Pursuant to N.J.S.A. 48:3-61(a)(1), the Board FINDS that the Company shall have the opportunity to recover such eligible stranded costs through the Company's Market Transition Charge, in a time frame and manner to be determined by the Board. The Board is not ruling on the amount of bondable stranded costs at this time. However, the Board emphasizes that, consistent with N.J.S.A. 48:3-

62(c)(1), in no event will the securitizable amount of any divested asset exceed 75% of the total amount of ACE's recovery-eligible utility generation plant stranded costs as determined by the Board in accordance with N.J.S.A. 48:3-61.

Finally, the Company maintains that, as a condition to closing of the purchase by NRG of the Fossil Assets, namely, Conemaugh, Keystone, B.L. England and Deepwater, NRG must qualify as an exempt wholesale generator[17], which will exempt NRG from regulation under PUHCA. Under Section 32 of PUHCA, certain generators of electricity may apply to the FERC to qualify for EWG status. In order for the Fossil Assets to be considered eligible facilities by FERC under Section 32 of PUHCA:

> (c) … every State commission having jurisdiction over any such rate or charge must make specific determination that allowing such facility to be an eligible facility (1) will benefit consumers, (2) is in the public interest, and (3) does not violate State law; [p]rovided, [t]hat in the case of such a rate or charge which is a rate or charge of an affiliate of a registered holding company:
>
> > (A) such determination with respect to the facility in question shall be required from every State Commission having jurisdiction over the retail rates and charges of the affiliates of such registered holding company….[15 U.S.C. §79z-5a(c)].

Because Conectiv is a registered holding company under PUHCA, and other states have jurisdiction over the retail rates and charges of the affiliates of Conectiv as of October 24, 1992 (the date of the enactment of Section 32 of PUHCA), each state commission having jurisdiction over the retail charges of the affiliates of Conectiv must make such determination with respect to all of the generation facilities being sold by Conectiv, regardless of the particular Conectiv affiliate owning such plants. By separate petition dated May 15, 2000, a Joint Application was filed with FERC by Conectiv and NRG seeking authorization for the sale of Conectiv's interest in the Fossil Assets to NRG.

For the reasons described above, ACE has requested that this Board make a specific determination that allowing the Fossil Assets, including Deepwater, to be "eligible facilities" pursuant to Section 32 of PUHCA will benefit consumers, is in the public interest and does not violate New Jersey law. Pursuant to Section 32(c)(A) of PUHCA, it appears that such a finding is required of this Board in order for the facilities to be considered eligible facilities under federal law.

Having reviewed the record in this matter, it appears that the sale of the Fossil Assets will not adversely affect either the availability or reliability of electric supply to ACE's customers and that reasonable generation asset divestiture should enhance the availability of competitive energy supplies in the northeast. Having reviewed NRG's assertions in the Joint Application to FERC, it does not appear that this transaction raises any significant generation or transmission market power issues within the State of New Jersey or PJM. Nevertheless, the Board, in conjunction with PJM, will closely monitor the potential for exercise of generation or transmission market power issues.

[17] Section 32(a) of PUHCA defines an EWG as "any person determined by the [FERC] to be engaged directly, or indirectly through one or more affiliates …, and exclusively in the business of owning or operating, or both owning and operating, all or part of one or more eligible facilities and selling electric energy at wholesale…."

Therefore, for the reasons stated, the Board HEREBY DETERMINES that allowing the Fossil Assets to be eligible facilities, pursuant to Section 32 of PUHCA, will benefit New Jersey consumers, is in the public interest and does not violate State law. The Board's determination is based on the facts of this transaction as they have been presented and shall not be precedential for any such future requests, by this or any other company, for similar determinations for other facilities.

DATED: February 20, 2002

BOARD OF PUBLIC UTILITIES
BY:

(SIGNED)

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ACTING PRESIDENT

(SIGNED)

FREDERICK F. BUTLER
COMMISSIONER

(SIGNED)

CAROL J. MURPHY
COMMISSIONER

(SIGNED)

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